

IN THE COURT OF APPEALS OF TENNESSEE
AT NASHVILLE
April 10, 2007 Session

COLONIAL PIPELINE COMPANY v. JOHN G. MORGAN, ET AL.

Appeal from the Chancery Court for Davidson County
No. 05-748-IV Richard H. Dinkins, Chancellor

No. M2006-00591-COA-R3-CV - Filed on July 2, 2007

Colonial Pipeline Company, an interstate common carrier and transporter of refined petroleum products, appeals the dismissal of its constitutional challenges to portions of Tennessee's tax system. The Chancery Court dismissed the Complaint on the basis that Colonial failed to exhaust its administrative remedies. Finding that declaratory judgments against the State are permissible in certain circumstances such as the ones presented here and that the nature of Colonial's claim relieved it of any obligation to exhaust its administrative remedies, we reverse.

**Tenn. R. App. P. 3 Appeal as of Right; Judgment of the Chancery Court
Reversed**

FRANK G. CLEMENT, JR., J., delivered the opinion of the court, in which WILLIAM C. KOCH, P.J., M.S., and PATRICIA J. COTTRELL, J., joined.

Ron L. Quigley, Atlanta, Georgia, and Stephen H. Price, Nashville, Tennessee, for the appellant, Colonial Pipeline Company.

Robert E. Cooper, Jr., Attorney General and Reporter; and Mary Ellen Knack, Assistant Attorney General, for the appellees, John G. Morgan, Tennessee Comptroller of the Treasury, et al.

OPINION

Colonial Pipeline Company is challenging what it describes as Tennessee's "famously dysfunctional" tax structure. The defendants in this action are John Morgan, the Comptroller of the Treasury for the State of Tennessee, the State Board of Equalization, Governor Phil Bredesen in his capacity as a member and Chairman of the State Board of Equalization, Secretary of State Riley Darnell, in his capacity as a member and Vice-Chairman of the State Board of Equalization, Loren Chumley, the Commissioner of Revenue in her capacity as a member of the State Board of Equalization, Doyle Arp, the Assessor of Property of the State of Tennessee, in his capacity as a member of the State Board of Equalization, and J.M. Bailey, a member of the State Board of Equalization.

The statutory scheme at issue classifies Colonial as a public utility for tax purposes, which requires that Colonial be assessed by the Office of State Assessed Properties, rather than by local county assessors. Tennessee classifies Colonial's mains, pipes, pipelines and tanks that are used to transport its products as real property¹ rather than personal property. This classification resulted in Colonial being taxed at a higher rate than some of its competitors whose properties were classified differently.

This is not the first challenge of the statutory tax scheme by Colonial. In 1997, Colonial challenged the statutory classification of Colonial as a public utility for tax purposes, which challenge made its way to this Court and resulted in a favorable ruling. In that matter, we determined that Colonial's pipeline and surface equipment should be treated as personal property for purposes of ad valorem taxes. See *ANR Pipeline Co. v. Tenn. Bd. of Equalization*, 2002 WL 31840689 (Tenn. Ct. App. Dec. 19, 2002).

Following our opinion in *ANR Pipeline Co.*, the General Assembly amended the statute and classified all mains, pipes, pipelines, and tanks as real property for tax purposes with the enactment of Chapter 719 of the 2004 Public Acts of the State of Tennessee. Tenn. Code Ann. § 67-5-501(9) (2004).

In the present action, Colonial filed a two-count Complaint. In Count 1, Colonial contends the classification in Chapter 719 constitutes a property classification that is "arbitrary, invidiously discriminatory, and is without rational relation to any legitimate government interest," which violates the equal protection clause of the U.S. and Tennessee Constitutions. Colonial also contends the discriminatory nature of the classification results in an undue burden on interstate commerce in violation of the Commerce Clause.

In Count 2 of the present action, Colonial contends the property classifications in two provisions of Article II of the Tennessee Constitution, § 28 REAL PROPERTY, Sub-classification (a) and § 28 TANGIBLE PERSONAL PROPERTY, Sub-classification (b), combine to violate the United States Constitution by operating to deny Colonial equal protection and result in an undue burden on interstate commerce by arbitrarily classifying the property as "Public Utility Property." The effect is that Colonial's real and personal property is assessed at 55%, while property of its competitors is classified as "Industrial, Commercial Property" which is assessed at lesser values, 40% for real property and 30% for personal property.

In this action, Colonial seeks, inter alia, to: (1) permanently enjoin the defendants from applying and enforcing the statutes that classify Colonial's property as real property and as a public utility property for ad valorem tax purposes; and (2) to declare Tenn. Code Ann. § 67-5-501(9) and the property classifications under the Tennessee Constitution distinguishing real and personal property unconstitutional.

¹For the definition and a complete listing of the property subject to classification as real property see Tenn. Code Ann. § 67-5-501(9).

The defendants filed a Motion to Dismiss contending, *inter alia*, Colonial had not exhausted its administrative remedies. The State argued that Colonial should have taken its complaint to the State Board of Equalization (the Board), and that only after exhausting the options with the Board, would it be appropriate to pursue the action in the Chancery Court. The defendants also moved for dismissal for want of subject matter jurisdiction because the Complaint against the Comptroller, State Board of Equalization, and members of the Board is a suit against the State, which is not authorized by law. The Chancellor granted the Motion to Dismiss, but only addressed the issue of administrative remedies; thus, we have no way of knowing if the Chancellor considered the subject matter jurisdiction issue.

Colonial contends the dismissal for failure to state a claim was error because: (1) the Board is biased and, therefore, cannot provide Colonial due process through a fair and impartial administrative review; (2) the Board does not have the authority to adjudge facial or “as applied” constitutional challenges to the relevant statute and thus Colonial was not required to exhaust administrative remedies; (3) Colonial was not required to exhaust administrative remedies because the issues raised are purely legal and requiring Colonial to go to the Board would be requiring them to engage in a useless act.

Colonial contends its claims for injunctive and declaratory relief are not claims against the state but are instead actions challenging the federal and state constitutionality of a statute and are therefore permissible.

STANDARD OF REVIEW

Despite the defendants filing their Motion to Dismiss pursuant to Tenn. R. Civ. P. 12.02(6) for failure to state a claim upon which relief can be granted, the Chancery Court dismissed Colonial’s Complaint after reviewing “the entire record in this case.” The consideration of evidence beyond the face of Colonial’s Complaint necessitates us treating this as a summary dismissal pursuant to Tenn. R. Civ. P. 56.²

Summary judgments are proper in virtually all civil cases that can be resolved on the basis of legal issues alone, *Byrd v. Hall*, 847 S.W.2d at 210; *Pendleton v. Mills*, 73 S.W.3d 115, 121 (Tenn. Ct. App. 2001); however, they are not appropriate when genuine disputes regarding material facts exist. Tenn. R. Civ. P. 56.04. The party seeking a summary judgment bears the burden of demonstrating that no genuine disputes of material fact exist and that party is entitled to judgment as a matter of law. *Godfrey v. Ruiz*, 90 S.W.3d at 695. Summary judgment should be granted at the

²“If, on a motion asserting the defense numbered (6) to dismiss for failure to state a claim upon which relief can be granted, matters outside the pleading are presented to and not excluded by the court, the motion shall be treated as one for summary judgment . . .” Tenn. R. Civ. P. 12.02. The trial court in its Final Order stated it considered “the entire record in this case.” The record contains numerous affidavits, excerpts from depositions, Defendants’ Statement of Material Facts submitted pursuant to Tenn. R. Civ. P. 12.02(6) and 56.03, and Colonial’s Response to Defendants’ Statement of Material Facts. Because the trial court considered matters outside the pleadings, the order resulting from the motion to dismiss must be reviewed as one for summary judgment.

trial court level when the undisputed facts, and the inferences reasonably drawn from the undisputed facts, support one conclusion, which is the party seeking the summary judgment is entitled to a judgment as a matter of law. *Pero's Steak & Spaghetti House v. Lee*, 90 S.W.3d 614, 620 (Tenn. 2002); *Webber v. State Farm Mut. Auto. Ins. Co.*, 49 S.W.3d 265, 269 (Tenn. 2001). The court must take the strongest legitimate view of the evidence in favor of the non-moving party, allow all reasonable inferences in favor of that party, discard all countervailing evidence, and, if there is a dispute as to any material fact or if there is any doubt as to the existence of a material fact, summary judgment cannot be granted. *Byrd v. Hall*, 847 S.W.2d at 210; *EVCO Corp. v. Ross*, 528 S.W.2d 20 (Tenn. 1975). To be entitled to summary judgment, the moving party must affirmatively negate an essential element of the non-moving party's claim or establish an affirmative defense that conclusively defeats the non-moving party's claim. *Cherry v. Williams*, 36 S.W.3d 78, 82-83 (Tenn. Ct. App. 2000).

ANALYSIS

In the Motion to Dismiss, the State contended that Colonial's action against the State could not be maintained for two reasons. One, Colonial failed to exhaust its administrative remedies. Two, a petition for Declaratory Judgment could not be maintained against the State.

The Chancery Court dismissed the action upon a finding that Colonial failed to exhaust its administrative remedies without addressing the second issue raised by the State, that being whether a petition for Declaratory Judgment could not be maintained against the State. We will address both issues.

Petition for Declaratory Judgment

The State relies on a line of cases, specifically, *Hill v. Beeler*, 286 S.W.2d 868, 871 (Tenn. 1956); *Northern Telecom Inc. v. Taylor*, 781 S.W.2d 837 (Tenn. 1989); *Carter v. McWhorter*, 859 S.W.2d 343 (Tenn. Ct. App. 1993), each of which held that the respective plaintiffs' actions could not proceed against the State pursuant to the Declaratory Judgment Act. We, however, have concluded that the foregoing cases are inapplicable to the type of action at issue, and that a separate line of cases controls which permits the filing of actions for Declaratory Judgment against the State provided the constitutionality of a statute is at issue. See *Richardson v. Tenn. Bd. of Dentistry*, 913 S.W.2d 446 (Tenn. 1995); *Campbell v. Sundquist*, 926 S.W.2d 250, 257 (Tenn. Ct. App. 1996).

Although our courts have held that the Declaratory Judgment Act "should be liberally construed in favor of the person seeking relief in a proper case to the end that rights and interests be expeditiously determined," there are limitations to the types of actions that can be brought under the Act. See *Campbell*, 926 S.W.2d at 256 (citing *Tenn. Farmers Mut. Ins. Co. v. Hammond*, 290 S.W.2d 860, 862 (Tenn. 1956)). One such limitation is a prohibition on actions against the State or

state officials where the goal is "to reach the state, its treasury, funds or property." *Campbell*, 926 S.W.2d at 256 (citing Tenn. Code Ann. 20-13-102(1992)).³

In *Campbell*, the State sought to dismiss the action by relying, as it is here, on *Hill*, *Northern Telecom*, and *Carter*. The *Campbell* court, however, found the State's reliance on *Hill*, *Northern Telecom*, and *Carter* misplaced. *Campbell*, 926 S.W.2d at 257. As the Court explained in *Campbell*:

The Declaratory Judgment Act expressly provides that courts are empowered to declare rights under, and construe, statutes. *Hill*, *Northern Telecom*, and *Carter* are inapplicable to the declaratory judgment question presented by the case before us. In all three of these cases in which the Courts held that the respective plaintiffs' actions could not be maintained under the Declaratory Judgment Act, the plaintiffs' actions were designed, in some fashion or other, to reach the state treasury, state funds, or state property, and thus the actions were clearly barred by T.C.A. § 20-13-102. In the instant case, the plaintiffs do not seek to reach the state treasury, funds, or property, and therefore, this case is distinguishable from the line of cases cited by the appellants.

Campbell, 926 S.W.2d at 257. As the *Campbell* court noted, the plaintiff in *Hill* was seeking an award from the State for the death of her husband, the plaintiff in *Carter* was seeking payment of a police pay supplement, and the plaintiff in *Northern Telecom* was seeking a tax refund. *Id.*

In the case at bar, Colonial is not seeking to reach the state treasury, state funds, or state property. Instead, Colonial is seeking a declaratory judgment that the present tax scheme is unconstitutional. We therefore conclude that it is permissible for Colonial to commence and maintain this declaratory judgment action against the State.

We now turn our attention to the question of whether Colonial was required to exhaust all available administrative remedies before seeking judicial review.

Administrative Remedies

The State relies on *Thomas v. State Bd. of Equalization* coupled with Tenn. Code Ann. § 67-5-1328 to contend that Colonial was required to exhaust its administrative remedies prior to seeking judicial review. See *Thomas v. State Bd. of Equalization*, 940 S.W.2d 563, 566 (Tenn. 1997). In pertinent part, Tenn. Code Ann. § 67-5-1328 provides:

³For other limitations see *Standard Accident Ins. Co. v. Carvin*, 400 S.W.2d 235, 236 (Tenn. 1966) (holding that the courts may not entertain a suit under the Declaratory Judgment Act if it would require the court to investigate disputed facts); see also *Parks v. Alexander*, 608 S.W.2d 881, 891-92 (Tenn. Ct. App.1980)(holding that a justiciable controversy "is also a jurisdictional prerequisite to the maintenance of an action under the Act").

(a)(1) The state board of equalization shall proceed to examine such assessments as made by the comptroller of the treasury, and is authorized to increase or diminish the valuation placed upon any property valued by the comptroller of the treasury, and is further authorized to require of the comptroller of the treasury any additional evidence touching one (1) or more of the properties assessed, and shall consider such additional evidence so furnished in fixing the correct value of any property so assessed, and the assessments shall not be deemed complete until corrected and approved by the board; the board is authorized to call the comptroller of the treasury at any time to perform the duties imposed upon it; provided, that if the board so desires, it shall have the power, without referring any assessment to the comptroller of the treasury, to employ experts, accountants, and to call witnesses to testify upon any assessment certified to it by the comptroller of the treasury. The board shall have the same powers to compel attendance of witnesses, production of books, papers, and documentary evidence as is by this chapter given to the comptroller of the treasury.

(2) The board has the right to call upon the federal highway administration for any valuations of property in the office of the administration and evidence in possession of such administration in support of such valuations.

(b) All of the evidence thus acquired by the board shall be considered by it in addition to the evidence transmitted to it by the comptroller of the treasury in support of the assessment so fixed by the comptroller of the treasury.

(c) Any expense incurred by the board in calling for the additional proof as to the value of any property certified to it by the comptroller of the treasury shall be by the board certified to the commissioner of finance and administration and paid by the commissioner out of any moneys in the state treasury not otherwise appropriated.

Tenn. Code Ann. § 67-5-1328.

The State argues that the above statute provides for an administrative remedy and thus, according to the State's interpretation of *Thomas*, the mere presence of this administrative remedy creates a duty to exhaust that remedy. *See Thomas*, 940 S.W.2d at 566. The State's interpretation of *Thomas*, however, is not entirely accurate. As the court in *Thomas* explained: “[g]enerally, when a statute provides an administrative remedy, one must exhaust this administrative remedy prior to seeking relief from the courts. . . .” *Thomas*, 940 S.W.2d at 566 (emphasis added). The court, however, went on to explain, “In Tennessee, *exhaustion is not statutorily required unless the statute ‘by its plain words’ requires it.*” *Id.* (emphasis added). Having examined the “plain words” of Tenn. Code Ann. § 67-5-1328, we find the statute provides an administrative remedy, however, it does not require a party to exhaust administrative remedies through the State Board of Equalization prior to seeking judicial review of the questions at issue in this appeal.

Aside from the plain words of Tenn. Code Ann. § 67-5-1328, there are exceptions to the requirement to exhaust available administrative remedies prior to seeking judicial review. One such exception is where a party is challenging the validity of an ordinance or a statute that would be applied by the administrative agency making the decision. *See B.F. Nashville, Inc. v. City of Franklin*, No. M2003-00180-COA-R3-CV, 2005 WL 127082, at * 6 (Tenn. Ct. App. Jan. 21, 2005) (citing *Poteat v. Bowman*, 491 S.W.2d 77, 80 (Tenn. 1973)). Another is where the party seeking judicial review raises only questions of law rather than questions of fact. In such a circumstance, there is no obligation to exhaust administrative remedies. *See Bracey v. Woods*, 571 S.W.2d 828, 830 (Tenn. 1978) (citing *Rosewood, Inc. v. Garner*, 476 S.W.2d 273 (Tenn. Ct. App. 1972)); *see also Fentress County Bank v. Holt*, 535 S.W.2d 854 (Tenn. 1976). A third exception is where the pursuit of administrative relief would be futile or useless. *See B.F. Nashville*, 2005 WL 127082, at * 6 (citing *State v. Yoakum*, 297 S.W.2d 635, 642 (Tenn. 1956)).

The issues presented by Colonial concern legal challenges to the statutory scheme that characterize certain of Colonial's property as real property rather than personal property for tax purposes, and the validity of portions of the Tennessee Constitution that distinguish between real property and tangible personal property statutes, and portions of the Constitution of the State of Tennessee, each of which constitutes a question of law. Where a party's complaint raises primarily questions of law, the court is the appropriate body to adjudicate the issues, and, therefore, the complaining party is not required to exhaust its administrative remedies. *See Rosewood, Inc. v. Garner*, 476 S.W.2d 273, 276 (Tenn. Ct. App. 1971); *see also Richardson*, 913 S.W.2d at 452 (holding an agency is not authorized to consider the constitutionality of a legislative act, nor may it declare unconstitutional the statutes which it was created to administer or enforce). These limitations are based on the constitutional principle of separation of powers. *See Richardson*, 913 S.W.2d at 453 (citing *Williams v. Carr*, 404 S.W.2d 522 (Tenn. 1966) (stating that administrative agencies are part of the executive branch, and any statute by the legislative branch purporting to vest administrative agencies with the authority to determine the constitutionality of statute violate the separation of powers doctrine)).⁴

⁴Tennessee, however, has recognized that agencies must "consider and apply constitutional principles in determining procedures and rendering decisions in contested cases." *Richardson*, 913 S.W.2d at 453 (citations omitted). The constitutional issues that a state agency may consider include "procedural constitutional issues that may arise in the context of a contested case." *Richardson*, 913 S.W.2d at 454. If the aggrieved party is presenting "an 'as applied' challenge to the constitutionality of a statute or any challenge to the constitutionality of an agency rule, the agency may initially rule on the challenge." *Id.* at 455. The agency may also address a claim "that an agency's procedure is constitutionally deficient." *Id.* The constitutional issues that are solely within the jurisdiction of the judicial branch involve "constitutional challenges to the statutes creating the agency and defining its subject matter and authority." *Id.* at 454. "The facial constitutionality of a statute may not be determined by an administrative tribunal in an administrative proceeding." *Id.* Although a state agency may consider as-applied constitutional challenges and constitutional challenges to agency procedures, consideration by the agency is not a mandatory prerequisite to seeking review of the issues in a Chancery Court. "The declaratory judgment and judicial review provisions [of the Administrative Procedures Act] do not require that constitutional issues be raised at the agency level," and "[t]he statutes clearly contemplate that in a number of circumstances, constitutional issues may be raised and addressed for the first time in chancery court." *Richardson*, 913 S.W.2d at 456. Although certain constitutional issues may be considered by a state agency, "the failure to raise these constitutional issues before the agency will not preclude a party in a contested case from raising the issue (continued...)

Colonial challenges Chapter 719 of the 2004 Public Acts of the State of Tennessee, which is now codified at Tenn. Code Ann. § 67-5-501(9), which as amended classifies all mains, pipes, pipelines, and tanks as real property for tax purposes. Tenn. Code Ann. § 67-5-501(9)(B)(iii). Colonial contends this classification is “arbitrary, invidiously discriminatory, and is without rational relation to any legitimate government interest,” which violates the equal protection clause of the U.S. and Tennessee Constitutions. Colonial also contends the discriminatory nature of the classification results in an undue burden on interstate commerce in violation of the Commerce Clause. This is a facial challenge⁵ to the constitutionality of this statute, and as such, this issue “may *not* be determined by an administrative tribunal in an administrative proceeding.” *Richardson*, 913 S.W.2d at 454.

The exhaustion of administrative remedies doctrine serves “to prevent premature interference with agency processes, so that the agency may (1) function efficiently and have an opportunity to correct its own errors; (2) afford the parties and the courts the benefit of its experience and expertise without the threat of litigious interruption; and (3) compile a record which is adequate for judicial review.” *Thomas*, 940 S.W.2d at 566. Colonial has not alleged that the State Board of Equalization made an error that it has the ability to correct. Therefore, requiring that Colonial return to the Board would not give the Board an opportunity to correct an error.

For the above stated reasons, we respectfully reverse the decision of the Chancery Court.

IN CONCLUSION

The judgment of the trial court is reversed, and this matter is remanded to the Chancery Court for further proceedings consistent with this opinion. Costs of appeal are assessed against the State Board of Equalization.

FRANK G. CLEMENT, JR., JUDGE

⁴(...continued)
for the first time upon judicial review.” *Richardson*, 913 S.W.2d at 458.

⁵At oral argument in this matter counsel for Colonial conceded that when the General Assembly amended the statute and classified all mains, pipes, pipelines, and tanks as real property for tax purposes with the enactment of Chapter 719 of the 2004 Public Acts of the State of Tennessee, Colonial’s as-applied challenge was rendered non-justiciable, leaving only facial challenges.